

## **FAIR POLITICAL PRACTICES COMMISSION**

### **Memorandum**

**To:** Chairman Getman and Commissioners Downey, Knox, and Swanson

**From:** C. Scott Tocher, Commission Counsel  
Luisa Menchaca, General Counsel

**Re:** Petition to Reconsider Regulation 18531.7 - Payments for Member Communications

**Date:** September 19, 2002

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### **I. INTRODUCTION**

At its August 2002 Commission meeting, the Commission adopted regulation 18531.7, interpreting and applying the membership communication provisions of section 85312. The California Federation of Labor, AFL-CIO, the California State Council of Service Employees International Union, and the California Teachers Association, petitioned after that meeting for reconsideration of the regulation, and proposed amendments thereto. (Ex. 1.) At the September meeting, the Commission granted the petition, withdrew regulation 18531.7, and scheduled consideration of the substance of the proposed changes for the October meeting.

This memorandum analyzes the proposed amendments and, where appropriate, makes recommendations to the Commission. In certain circumstances, staff has offered alternative language to that proposed in the petition. (Reg. 18531.7 attached as Ex. 2; staff suggestions in "SMALL CAPS".) Rather than address the proposed amendments strictly in order of appearance in the text of the regulation, the discussion below is organized by the subject areas which are addressed by the amendments. It is hoped that organization in this manner will better facilitate a seamless flow of the discussion. Within each subject area, the discussion is broken down into sections addressing current law (as embodied in the regulation adopted by the Commission in August), the proposed amendments, and finally the staff's recommendation.

### **II. PETITION AMENDMENTS**

It is important to make clear from the outset that the petition for reconsideration does not advocate a permanent repeal of regulation 18531.7 as adopted by the Commission in August. Rather, the proposal sets forth amendments in four substantive areas of the regulation.<sup>1</sup> Each proposed amendment, however, expands the reach of the

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<sup>1</sup> As a procedural matter, because the regulation adopted by the Commission at the August meeting would have gone into effect before reconsideration could have been accomplished, the

membership communication exception, to which, generally speaking, the Commission gave a narrow interpretation. In considering each amendment, one must consider the relevant issue not in isolation but in its entirety with respect to the other aspects of the regulation, as well.

As a preamble to the discussion below, it is helpful to be reminded that payments for communications supporting or opposing a candidate or ballot measure typically are reportable "contributions" or "expenditures" under the Political Reform Act (the "Act").<sup>2</sup> (§§ 82015 and 82025.)<sup>3</sup> Section 85312, enacted by Proposition 34 and later amended by Senate Bill 34, provides an exception to this general rule for "member communications."<sup>4</sup> If an entity raises or expends \$1,000 or more with respect to a candidate or ballot measure, then that entity becomes a "committee." Once it is established, the committee must comply with the Act's rules regarding disclosure of contributions and expenditures and make periodic public filings. In addition, contributions the committee may make to a candidate are subject to limitation. Thus, section 85312, by carving out an exception for payments that otherwise would be considered a "contribution" or "expenditure," operates to prevent certain entities from becoming subject to the Act's rules described above.

As amended, section 85312 provides:

"For purposes of this title, payments for communications to members, employees, shareholders, or families of members, employees, or shareholders of an organization for the purpose of supporting or opposing a candidate or a ballot measure are not contributions or expenditures, provided those payments are not made for general public advertising such as broadcasting, billboards, and newspaper advertisements. However, payments made by a political party for communications to its members who are registered with that party which would otherwise qualify as contributions or expenditures shall be reported in accordance with Article 2 (commencing with Section 84200) of Chapter 4, and Chapter 4.6 (commencing with Section 84600), of this title."

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Commission withdrew regulation 18531.7 from the Office of Administrative Law ("OAL"). On September 12, 2002, the OAL notified the Commission that the regulation was withdrawn pursuant to the Commission's request.

<sup>2</sup> All references are to the Government Code.

<sup>3</sup> Sections 82015 and 82025 provide the definitions for contribution and expenditure, respectively. These sections are further interpreted by regulations 18215(a)(1) and 18225(a)(1).

<sup>4</sup> "Member communications" refers to communications to members, employees, and shareholders of an organization or families of those persons and is the colloquial name given to the provisions of section 85312.

**A. Sponsored Committees (Decision 1):**

The petition proposes amending subdivisions (a) and (d) of the regulation to provide that payments made by an organization's sponsored committee to the organization's members are covered by section 85312 (meaning they are protected "membership communications" not subject to limit).

A "sponsored committee" is most commonly thought of as a committee that receives 80% or more of its contributions from a single source or organization. In fact, that is but one of four methods by which a committee may qualify as a "sponsored committee." Section 82048.7 defines a "sponsored committee" as follows:

**"§ 82048.7. Sponsored Committee.**

(a) 'Sponsored committee' means a committee, other than a candidate controlled committee, which has one or more sponsors. Any person, except a candidate or other individual, may sponsor a committee.

(b) A person sponsors a committee if **any** of the following apply:

(1) The committee receives 80 percent or more of its contributions from the person or its members, officers, employees, or shareholders.

(2) The person collects contributions for the committee by use of payroll deductions or dues from its members, officers, or employees.

(3) The person alone or in combination with other organizations, provides all or nearly all of the administrative services for the committee.

(4) The person, alone or in combination with other organizations, sets the policies for soliciting contributions or making expenditures of committee funds." (Emphasis added.)

Thus, as shown above, a sponsored committee that has qualified under subdivisions (2) through (4) may solicit and receive contributions of unlimited amounts from third parties and remain a "sponsored committee" under this definition.

**1. Current Law:**

Whether in fact an organization may use, under the adopted version of the regulation, sponsored committee funds is dependent upon how the sponsored committee is itself organized. In point of fact, the regulation does not prevent, across the board, sponsored committee funds from being used for membership communications. Rather, the Commission determined in August that a sponsored committee, for purposes of determining its "members," would be treated as any other organization under the regulation. That is, the sponsored committee is free to make payments for

communications to the committee's members as defined in subdivision (a)(2) of the regulation - those who have rights of participation in the committee. If the sponsored committee is so organized, the sponsored committee may expend resources in communicating with those members and be protected by section 85312.

The Commission's decision not to treat sponsored committee funds different from other organizations was based in part on several considerations. First, the Commission did not wish that committees and non-committees define "members" differently. The Commission expressly rejected the notion that mere contributions to a committee, of any type, would be sufficient to establish membership. Also informing the Commission's determination was the desire to avoid creating loopholes in the overall contribution-limited electoral scheme. By treating sponsored committee funds as that of any other committee and organization, the regulation avoided creating an incentive to manipulate the flow of campaign contributions to avoid detection and limit.

## **2. Proposed Amendments:**

It is brought to the Commission's attention, however, that certain organizations, for tax purposes, communicate using the organization's sponsored committee funds rather than general fund resources. (Public Comments of K. Donovan, Esq., at Comm'n. mtg, 9/5/02.) It also is argued that distinguishing payments to an organization's members on the basis of which "bank account" holds the funds is not necessary. (L. Olson, Esq., ltr. to Comm'n., 9/3/02; Ex. 3.)<sup>5</sup>

The essential result of the amendments to subdivisions (a) and (d) proposed in the petition would mean that sponsored committee funds could be used for communications to members of the *sponsoring organization*, rather than only members of the *sponsored committee*.

## **3. Staff Recommendation (Decision 1):**

Staff is not unsympathetic to real-world dilemmas that face organizations that wish to communicate to members using sponsored committee funds. Staff believes that most Commission concerns may be protected while accommodating the petition's request, with some revisions.

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<sup>5</sup> The petition of 8/22/02 also avers the regulation is internally inconsistent on this issue. The petition states that subdivision (f)'s reference to committees as defined by section 82013, subdivision (a), suggests that "sponsored committee payments can qualify under section 85312, but they simply must be reported." (Ex. 1 at p. 3.) Staff disagrees that the regulation is inconsistent or unclear. A committee as defined by subdivision (a) of section 82013 *may* include, but does not necessarily include, a sponsored committee. That subdivision also includes general purpose committees and primarily formed committees, for instance, that are non-sponsored. In addition, as discussed earlier, sponsored committees are not excluded from section 85312. Assuming they meet the membership requirements of any other organization, those expenditures to their "members" will fall under the scope of section 85312. Subdivision (f) merely indicates how, when they do fall under section 85312, they must be reported.

**Staff recommends the Commission reject amendment to subdivision (a), but staff agrees that the Commission should augment the proposed amendment to subdivision (d) with additional language.** Staff believes, in the absence of justification otherwise, that the reference to sponsored committees in subdivision (a) is unnecessary and potentially confusing. Rather, staff agrees that the petitioner's concerns are accomplished by the proposed amendment to subdivision (d). This subdivision provides the boundaries of the statute's reach and so this is the most logical placement for language regarding sponsored committees. Staff recommends augmenting the amendment with the bracketed language on line 7 of page 1 of Exhibit 2, to clarify that the earmarking language applies not only to contributions received by the organization but also its sponsored committee.

As applied with the proposed amendments, the new regulation would allow an organization to use money from its PAC to pay for communications to the organization's members. Also, in clarifying that the earmarking provisions of subdivision (d) apply to the sponsored committee's funds, staff believes an appropriate safeguard is preserved that prevents undue manipulation or circumvention of contribution limits. For instance, staff believes that, under the proposed amendments, a candidate and large contributor could not conspire to avoid limits to the candidate by funneling a large contribution by the donor to an organization's sponsored committee with the intent of funding a given communication to the organization's members.<sup>6</sup> Whatever the Commission decides later regarding cooperation between membership organizations and candidates, the Commission appropriately may draw a line at earmarked contributions by third parties to a sponsored committee.

A final issue of which to be mindful: it is generally thought that because committees (except political party committees) are subject to contribution limits of \$5,000 per calendar year, (section 85301, subd. (a)), the system itself is protected from enormous contributions by third parties to membership organizations in order to avoid contribution limits to the candidate by the large donor. In point of fact, however, the limit on contributions to committees *only* applies to contributions "for the purpose of making contributions to candidates for elective state office." From this language, one may make two important observations. First, the \$5,000 contribution limit does not apply to contributions to committees for the purpose of making contributions to candidates *other than* those for elective state office. Those, presumably, are unlimited. Second, if a contribution is earmarked for an organization's membership communications, then the case may be made that the contribution is *unlimited* because section 85301's express terms apply only to the committee's use of the funds for the purpose of making "contributions" to candidates. Because section 85312 declares membership communications are not "contributions," then it may be argued that contributions to a sponsored committee for purposes of membership communications are unlimited. Such an outcome, if true, reinforces maintaining a ban on use of third-party funds for member communications even when paid for by a sponsoring committee.

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<sup>6</sup> Under existing provisions, the PAC in this scenario already must report receipt of the contribution from the third party. The payment by the PAC for the membership communication would be reported pursuant to subdivision (f) of regulation 18531.7.

**B. Definition of "member": (Decision 2)**

The petition proposes adding language to subdivision (a)(2) to expand the definition of "member." Of course, by expanding the definition of "member" the amendments expand the reach of section 85312 from that given by the Commission in the version of the regulation adopted in August.

**1. Current Law:**

When the Commission adopted the narrower definition of "member," it considered and rejected broader forms. Even with the narrower definition, however, the Commission intended to reach and include labor and trade groups within the ambit of the regulation. In fact, the Commission asked that the public inform the Commission should the regulation fail in some regard to reach those organizations as a result of the narrow definition of "member."

Chief among the distinguishing characteristics for the Commission in its definition of "member" was the requirement of some form of participatory right in the stewardship of the organization itself. It is this fundamental aspect which separates traditional membership organizations from purely commercial ones. It also is on this basis that the Commission expressly rejected expanding the reach of the statute to include purely commercial enterprises that might in some fashion charge a "membership" fee, such as video rental stores, grocery stores, and large bulk stores such as Costco.

**2. Proposed Amendments:**

The petition proposes amendments to subdivision (a)(2) for several purposes. The amendment at line 17 to add "directly or indirectly" expands the definition to provide for certain organizational structures found in the real world whereby the election of directors is done indirectly by the membership. (Ex. 2, p. 1, Line 17.) The additional language on line 18 of the subdivision expands the definition to reach those groups whose members may elect an officer of the organization, as opposed only to the election of the directors of an organization. (*Id.*, at Line 18.) This language, virtually identical to language in a similar federal regulation, seeks to reflect more accurately the actual structure of certain organizations that the regulation presumably intends to reach. The third proposed amendment would provide a separate qualifying condition for membership: the payment of annual dues as required by the organization. (*Id.*, at Line 22.) Finally, a last sentence is proposed to clarify that members of local unions are considered members of any national or international union that is a part of or affiliated with the local union. (*Id.*, p.1, Line 23; P.2, Lines 1-2.)

**3. Staff Recommendation (Decision 2):**

**With respect to the amendments proposed by the petition at lines 17, 18 and 23, which pertain to indirect elections, the elections of officers and the membership in affiliated unions, staff recommends the Commission adopt these amendments.** Staff

believes these amendments are consistent with the spirit and letter of section 85312 and the intent of the Commission to include such organizations when it set about in August to define the term "member."

**Staff recommends the Commission reject the proposed amendment at line 22 to establish a separate single factor to define member solely on the basis of the payment of dues.** Other than argument contained in a footnote to the petition, petitioners offer no meaningful explanation to justify such an unnecessary expanse to the reach of the statute to purely commercial endeavors. For instance, the petition points to no actual union or trade organization that would be excluded without the offered language.

Rather, staff continues to believe in the correctness of the Commission's decision to reject similar language that was considered in August. No matter the window dressing afforded by calling someone a "member," customers of business enterprises are simply that: customers. From a constitutional perspective, nothing in the case law regarding the protection of membership communications as First Amendment activity requires or even justifies application of section 85312 in such commercial contexts. Moreover, nothing in the statute itself counsels such expansion: the language of the statute explicitly sets forth the limited circumstances of its application: shareholders and employees. If the voters wished to exempt business-to-consumer communications they could have done so - the fact they did not do so is instructive.

Finally, on the ground petitioners call "least justifiable" - the "unlikely" event that a commercial enterprise will mail to "members" its views in an upcoming election - the Commission's wisdom is proven correct. As indicated in the attached news article, (Exhibit 4), a mailing to Sam's Club customers in North Carolina containing an article featuring North Carolina Senate candidate Elizabeth Dole and her campaign photo is the subject of an FEC complaint. Wal-Mart's political action committee, the parent of Sam's Club, already had contributed the maximum amount to the Dole campaign. The estimated value of the mailing to the 200,000 residents of North Carolina is \$2,000,000. A spokesperson for the Dole campaign disputed the allegation that the article and its timing were "political," but maintained that even if it were "political" it was "perfectly legal" because it was a mailing to members of an organization. Whatever the merits of the complaint in the context of the broader regulation adopted by the FEC, staff sees no reason - practical, legal or otherwise - for opening up California's elections to the same potential for mischief as may have happened in the federal context.

### **C. Communications Made at the Behest of Candidates: (Decision 3)**

Petitioners next challenge the Commission's determination, as provided in subdivision (e) of the regulation, that membership communications made "at the behest" of a candidate are not entitled to the exemption afforded by section 85312. (Ex. 2, p.3, Lines 13-14.)

## 1. Current Law and the Proposed Amendment:

As embodied in subdivision (e) of the regulation, the Commission determined in August that payments made at the behest of a candidate for membership communications are in fact contributions. This scenario does not contemplate participation of third parties, as in subdivision (d) of the regulation, but instead addresses the scenario whereby a candidate asks an organization to communicate to its members regarding the candidate or his or her opponent.

The Commission based this decision on a concern that the broader contribution limits would be thwarted were candidates allowed to work closely with membership organizations to communicate to their members about the candidate. What the organization is prohibited (or in limited fashion) from doing directly, the argument goes, it should be prohibited from doing indirectly. That is, direct support of a candidate in the form of a contribution is limited. Therefore, indirect support of a candidate through communications to others may similarly be limited.<sup>7</sup>

The proposed amendment reverses this decision. While there is no direct case law on this point, staff is persuaded by principles of statutory construction and interpretation that section 85312 intended to allow membership organizations to coordinate communications to their members with candidates.<sup>8</sup> The rationale for this argument is as follows: A payment for a communication made by an organization can only be one of two things: either an independent expenditure *or* a contribution. If there is coordination between the candidate and the organization, then it is a contribution. If no coordination exists, then the payment is an independent expenditure. Therefore, the *only* circumstance, before section 85312, in which a payment by a membership organization would have been considered a contribution would have been when it was made at the behest of the candidate. Thus, the only context in which section 85312 has application - the only time when a payment *would have been considered a contribution* - was precisely when there was coordination with a candidate. Accordingly, the only way to give meaning and effect to the statute is to conclude that it allows a candidate to coordinate an expenditure by an organization for purposes of communicating to that organization's members, shareholders, employees and families of those people.

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<sup>7</sup> See, for instance, the *Bell* Advice Letter, I-90-268 (Exhibit 5), in which Commission staff advised that where an individual member of an organization, at a candidate's behest, makes an expenditure to communicate with the organization's members, such would not be a communication between the organization and its membership. (Exhibit 5.) The letter goes on to conclude that the organization's mailing of envelopes in which the members are asked to return contributions for the candidate "is not a communication, but the provision of goods and services." Though not yet presented with such a question, staff believes this advice would continue to apply under section 85312 and regulation 18531.7.

<sup>8</sup> Federal law also allows, for instance, a union to coordinate with a candidate a member communication. (11 CFR § 114.2, subd. (c).) Political parties, however, must treat coordinated member communications as contributions to the candidate. (*See FEC v. Colorado Republican Federal Election Cmte* 533 U.S. 431, 121 S.Ct. 2351, 150 L.Ed.2d 461). Proposed regulation 18531.7 and section 85312 establish the same rules.



This concept works when the expenditure itself is considered an expenditure “by” an organization. Therefore, the question turns again to when is an expenditure by an organization an internal membership communication, versus an earmarked communication or a communication where the organization is a mere conduit or intermediary, which may result in contravention of the contribution and expenditure limits.

Provided the Commission retains subdivision (d) in its present form, the abuse the staff intended to prevent is significantly curtailed. There are still some questions that remain. For example, if a payment is made to a membership organization by a new member for a specific member communication, should that payment fall outside the exception? Staff believes the current language of subdivision (d) would allow a case-by-case interpretation of these questions and therefore can address many of the questions in the context of subdivision (d).

### **3. Staff Recommendation: (Decision 3)**

In light of the analysis above, **staff recommends the Commission delete subdivision (e), which pertains to communications made at the behest of candidates, in its entirety.** Staff believes the regulation flows in a less cluttered manner without the subdivision. If the Commission determines it wishes to maintain the subdivision, staff recommends the inclusion of the petition's proposed amendment to subdivision (e).

### **D. Reporting of Payments Covered by the Membership Communication Exemption: (Decision 4)**

#### **1. Current Law and the Proposed Amendment:**

Subdivision (f) of regulation 18531.7 governs how the expenditure of campaign funds by committees is to be reported. Payments made for member communications by these groups qualify for the exemption under section 85312 but still must be reported. The regulation requires that those payments be reported in accordance with the requirements of section 84211, subdivisions (b), (i), (j) and (k). These provisions govern the disclosure these committees make on their reports in other contexts in addition to member communications. Specifically, the regulation requires, by reference to subdivision (k) of section 84211, that committees disclose on their reports the date the payment is made and the candidate or ballot measure connected to the payment. (§ 84211, subd. (k)(5).)

This language follows up on earlier determinations made by the Commission with regard to member communications<sup>9</sup> and became the substance of staff advice in the

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<sup>9</sup> Earlier this year, staff advised the Commission that excluding committee payments for member communications from reporting would be troublesome. Section 84211, subdivision (e), requires committees to disclose the balance of cash held at the beginning and the end of each reporting period. The Form 460 is structured so that every dollar received and spent is disclosed on one of the form schedules. The total reported on each schedule is carried over to the campaign statement summary page, where the

Zakson Advice Letter, A-01-195. (Ex. 6.) In that letter, the issue was discussed as follows:

"With regard to committee reporting of payments for these communications, the Commission supported the approach of including committees as an 'organization' but requiring reporting of the payments made by a committee for membership communications in the same manner that expenditures are reported. (Minutes of the Meeting, March 14, 2002.) The proposed regulation considered by the Commission at the March 2002 meeting provides:

" '(d) If the organization is a committee organized under Government Code section 82103(a) and therefore already subject to the reporting requirements of Chapter 4 of this title, the payment is reportable as an expenditure in accordance with the requirements of Government code section 84211, subdivisions (b), (i), (j) and (k).' (Proposed Regulation 18531.7, considered at the March 2002 Commission Meeting.)

"The Commission's rationale for their support of this approach was based on the reporting provisions of Chapter 4 of the Act ('Campaign Disclosure'), requiring a committee to report all payments which it makes and receives. (See Memorandum to the Commission, 'Payments for 'Member Communications,' March 7, 2002; Sections 84200-84204, 84211; *Karnette* Advice Letter, No. I-87-192.) Specifically, section 84211(e) requires committees to disclose the balance of cash held at the beginning and the end of each campaign reporting period. Thus, in an effort to issue advice consistent with the Commission's preliminary determinations regarding section 85312, we advise a labor union which qualifies as a committee to report all payments made from the committee's funds, including those which may be covered by section 85312, in the manner described above." (Internal footnotes deleted.)

Accordingly, staff advised that the provisions of subdivisions (k)(1)-(5) would apply.

The proposed amendment deletes one important aspect of that reporting - the date a given payment is made and the *candidate or ballot measure* connected to the payment.

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committee uses these figures to calculate its cash balance at the end of the reporting period. For committees using software packages that provide both recordkeeping and reporting functions, excluding certain payments that must be used to calculate cash on hand balances will necessitate changes to software, and also perhaps to the Form 460 and the Secretary of State's electronic filing formats. Thus, staff advised, and the Commission concluded, that payments made by recipient committees for member communications could and should be reported. The Los Angeles City Ethics Commission, also, has indicated in the past its concern that failure to report this information would hamper efforts to disclose pertinent information in city elections.

(§ 84211, subd. (k)(5).) (Ex.2, p.3, Line 18.) The petition and follow-up correspondence by petitioners do not discuss the basis or reason for this amendment.

**2. Staff Recommendation: (Decision 4)**

**Staff recommends, in the absence of a compelling reason otherwise, to maintain current advice with respect to committee reports of membership communications and reject the petition's proposed amendment.** In the event the Commission adopts the proposed amendment, staff has included bracketed language it recommends be added to require that such payments be described as member communications on the campaign statement. (Ex.2, p.3, Lines 18-19.)

Attachments:

1. Petition for Reconsideration of 8/22/02.
2. Regulation 18531.7 with Petitioner's proposed language and staff amendments.
3. Olson letter to Commission of 9/3/02.
4. BNA article on Sam's Club mailer, 9/9/02.
5. *Bell* Advice Letter, I-90-268.
6. *Zakson* Advice Letter.